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Kirkland Alert

The EU Foreign Subsidies Regime: Final Implementing Regulation

11 July 2023

Summary

The final version of the EU Foreign Subsidies Regime ("**FSR**") Implementing Regulation (the "**Implementing Regulation**"), including the text of the notification forms, was adopted on 10 July 2023 and will be officially published on 11 July 2023. The Implementing Regulation encompasses the notification forms and sets out the procedural aspects of this new screening regime. Extensive push back from the business community on the scope of disclosure requirements envisaged in the draft implementing framework published in February 2023[1] has been reflected in some helpful concessions. There will still be a heavy lift for notifying parties (and target businesses) however and there is limited time to prepare before notifications become mandatory on 12 October 2023. Pre-notification discussions with case teams have the potential to become protracted as the regime becomes active and the practice and approach towards disclosures required to inform the European Commission's (the "**Commission**") analysis is worked out.

Key updates

We would highlight the following takeaways from the final version of the Implementing Regulation:

- The jurisdictional thresholds under the FSR remain unchanged, as these were set out in EU legislation (the FSR Regulation adopted in December 2022[2] (the "**FSR Regulation**")).

- Only the acquisition of control[3] of a target business (or joint venture) generating more than €500 million of revenue within the EU Member States[4] annually can trigger an FSR filing requirement — such transactions are likely to be a relatively limited subset of the deals, which qualify for EU merger control review.[5]
- Such acquisition will trigger an FSR filing requirement if the acquirer and / or the target business have received combined aggregate foreign financial contributions ("**Financial Contributions**")[6] exceeding €50 million in the last three years prior to the conclusion of the transaction agreement.
- A very broad range of Financial Contributions received from public bodies continues to count towards the €50 million jurisdictional threshold.[7] An assessment of receipt of Financial Contributions on a broad basis will therefore need to be carried out to determine whether FSR notifications are triggered. Such Financial Contributions would include (amongst other things):
  - Limited Partner investments by state/public bodies (widely defined) received in aggregate across all funds controlled by the same General Partner (although detailed disclosures may be more limited, as discussed below).
  - COVID era government loans and subsidies.
  - Ordinary course supply arrangements with any public sector providers, e.g., healthcare and education providers.

- Some important concessions have been made to the disclosure requirements in the FSR notification form (named the "**Form FS-CO**" for mergers)[8] with the intention of focussing disclosures on Financial Contributions, which are potentially distortive of competition (in line with the policy objectives of the FSR).
  - The *de minimis* threshold for disclosures (regardless of whether the Financial Contribution is likely to distort the internal market pursuant to the FSR)[9] has been amended, such that Financial Contributions, which are individually valued at less than €1 million per third country, will not require disclosure in the Form FS-CO, subject to certain exceptions.
  - There is no reporting requirement for Financial Contributions from third countries that are unlikely to distort the internal market where the estimated aggregate amount of all Financial Contributions granted in the three years prior to the signing of the transaction agreement[10] is below €45 million. This additional floor does not apply to Financial Contributions that are likely to distort competition in the internal market. For private equity fund acquisitions, disclosure will be limited to the acquirer fund(s) for the transaction, which triggers an FSR filing requirement, provided that:

    i) other funds controlled by the same General Partner have a majority of different investors, measured according to entitlement to profit;

ii) the acquirer fund is subject to Directive 2011/61/EU of 8 June 2011 on Alternative Investment Fund Managers or equivalent protective legislation; and

iii) there are no "economic and commercial transactions" between the acquirer fund and others controlled by the same General Partner.

PE sponsors will want to limit disclosures on this basis wherever possible and so there will be questions to work through with case teams on this.

- Ordinary course purchase and supply arrangements entered into on market terms with public bodies are also excluded from disclosure — this was a particular source of push back given the prevalence of public sector customers in certain sectors, such as healthcare. The Form FS-CO does however require disclosure of ordinary course financial services arrangements with public bodies and there is likely to be some discussion with case teams about what should be provided on this.
- Ordinary course deferrals of tax or of social security contributions, including tax amnesties and holidays, normal depreciation and carry forward of losses are not generally subject to disclosure. Only where such tax reliefs are focussed on specific sectors, regions or (certain types of) particular companies, will they need to be reported in the Form FS-CO. In addition, tax relief on the basis of double taxation treaties and unilateral tax relief for the avoidance of double taxation are not subject to disclosure (in the latter case, as long as it follows the same logic and conditions as tax relief based on bilateral or multilateral agreements).
- A reduced set of information is required on sale processes, in particular with respect to the number of potential bidders that participated in an auction sale and levels of interest at each stage in that process. Sales/due diligence materials and contact details for competing bidders no longer need to be provided. Whilst the information burden has been reduced, the relevant section of the Form FS-CO is still likely to require uncomfortable disclosures for sellers to describe sale process at a time when a signed transaction (subject to an FSR notification) has still not closed.

- The Commission highlights the possibility to seek waivers from disclosure requirements during pre-notification discussions and invites early engagement on this. In particular, the Commission is open to providing waivers for information, which is not "reasonably available" or "necessary for the Commission's examination of the case" (and no longer suggests that allowances for information, which is not reasonably available, will be exceptional). This is in line with Executive Vice President Vestager's recent announcement that the Commission "*would be prepared to make*

decisions based on the information available to it", although she also said that the Commission will have to see how it can "*push*" some parties subject to a notification requirement.[11] Whilst the final implementing framework generally sets a constructive tone, the fact that these conversations will only take place in pre-notification — typically after a deal has signed — means that there are no upfront guarantees on the scope of required disclosures.

- The FSR review process continues to be broadly aligned with EU merger control, such that Phase I clearances for straightforward cases should be expected within 25 working days of the clock starting on the formal review (i.e., after the pre-notification phase). In the early days of the FSR (in particular, during the remainder of 2023), there is a risk that pre-notification periods could run for longer for FSR notifications however, as there will be a need to discuss disclosure requirements for particular cases (and there is not yet any established practice on this). We understand that the merger control teams at the Commission will largely staff FSR review cases at the outset, as recruitment remains ongoing for the Commission's FSR team. We hope this is a sign that cases will be handled pragmatically and will benefit from best practices adopted in EU merger control reviews.

Required disclosures in the Form FS-CO

Detailed information on Financial Contributions in any of the following categories, which are considered likely to distort the internal market,[12] is required in the Form FS-CO (subject to any waivers granted by the case team in a particular case):

- any foreign subsidy directly facilitating a transaction (for obvious reasons, this is a focus of the FSR);
- foreign subsidies granted to an ailing business, which are likely to fail in the short or medium term. However, restructuring plans expected to lead to the long-term viability of a target business and which also include significant contributions from the recipient of the subsidy, are excluded from disclosure;
- unlimited guarantees for debts / liabilities (unlimited in amount or duration);
- export financing measures, which are not in line with the OECD supported export credits; and
- foreign subsidies enabling businesses to submit "unduly advantageous" tender proposals in order to win contracts.

For any other types of Financial Contributions, notifying parties will need to report a less detailed overview (in table format, covering the type of contribution, purpose,

granting entities and amount by each third country in the prior three years in a broad range) of Financial Contributions granted to the notifying party/ies over the last three years prior to signing of the transaction agreement,[13] of an individual amount of at least €1 million by each third country, subject to a number of exceptions. The notifying party/ies can exclude any third countries where the estimated aggregate amount of all Financial Contributions granted in the three years prior to the conclusion of the agreement is below €45 million — however, a calculation will need to be made to see if this applies (so whilst the disclosure requirements may be reduced on this basis, the information gathering burden may not be so much).

During the review process, the Commission can request additional information on any type of Financial Contribution if it considers such information necessary for its assessment.

In addition to tracking value of all Financial Contributions received to inform the jurisdictional analysis, preparations to be ready to submit FSR notifications as from October 2023 should therefore focus on gathering more detailed information on these types of Financial Contributions received over the last three years.

Next steps

Any deal, which closes after 12 October 2023, is subject to mandatory and suspensory prior approval under the FSR where the jurisdictional thresholds are met. Therefore, all transactions should now be checked for an FSR notification requirement (and made conditional on FSR approval, as required). As from 12 July 2023 (when the FSR will start to apply), the Commission can already intervene *ex officio*.

Acquirers should consider whether they are likely to acquire control of a target business or joint venture with revenues in excess of €500 million in the EU in the near future — if so, it would be prudent to start gathering information internally to be ready to confirm if the €50 million jurisdictional threshold, which captures Financial Contributions received by an acquirer and target business on a combined basis, is likely to be met on any deal and to be ready to make required disclosures in FSR notifications. Given the limitation of disclosures in the Form FS-CO to acquiring funds, PE sponsors may want to start gathering information on relevant Financial Contributions received by portfolio companies of flagship funds, who are likely to be making sizeable acquisitions in the EU.

Acquirers, who are unprepared and therefore will require some time to confirm whether a FSR filing requirement applies for any transaction and/ or to prepare an FSR notification, may be disadvantaged in sales processes, relative to acquirers, who are ready to move quickly on this.

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1. See our *Alert* of 8 February 2023, which includes further detail on the procedural aspects of and substantive assessment pursuant to the FSR, available at www.kirkland.com/publications/kirkland-alert/2023/02/eu-foreign-subsidies-regime-draft-implementing-regulation. ↩

2. Regulation (EU) 2022/2560 of the European Parliament and of the Council of 14 December 2022 on foreign subsidies distorting the internal market. ↩

3. Minority interest acquisitions, which do not give rise to control (i.e., the ability to exercise decisive influence), do not trigger FSR notifications, consistent with the approach taken under EU merger control rules. ↩

4. As per Article 20(3)(b) FSR Regulation. Noting that UK revenues no longer count towards this threshold. ↩

5. In the case of a joint venture, the joint venture itself would need to be established in the EU and generate revenues in excess of €500 million to prompt an FSR filing requirement (fewer joint venture transactions will require FSR approval than EU merger control approval therefore). ↩

6. As defined in Article 3(2) FSR Regulation. Financial contributions are distinguished from subsidies, as they do not presuppose that the recipient received an advantage. ↩

7. As per Article 20(3)(b) FSR Regulation. ↩

8. The equivalent name for FSR public procurement notification forms is Form FS-PP. ↩

9. According to Article 5(1) FSR Regulation. ↩

10. Or the announcement of a public bid or the acquisition of a controlling interest. ↩

11. Executive Vice President M. Vestager, comments of 27 June 2023, as reported by news service PaRR. ↩

12. According to Article 5(1) FSR Regulation. ↩

13. Or the announcement of a public bid or the acquisition of a controlling interest. ↩

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Suggested Reading

- 11 July 2023 Press Release Kirkland Advises Nordic Capital on Sale of Bladt Industries to CS Wind
- 06 July 2023 Kirkland Alert Dramatic Overhaul Proposed to Hart-Scott-Rodino Pre-Merger Form
- 23 June 2023 Press Release Kirkland Represents Banyan Acquisition Corporation on Business Combination with Pinstripes, Inc.